United States Court of Appeals

for the Second Circuit

APPELLEE’S BRIEF

UNITED STATES COURT OF APPEALS
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SECOND CIRCUIT

75-7008

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To be argued by
PETER FLEMING JR.

United States Court of Appeals

FOR THE SECOND CIRCUIT

STUART A. JACKSON,

Plaintiff-Appellant,

—v.—

JACK OPPENHEIM,

Defendant-Appellee.

BRIEF OF DEFENDANT-APPELLEE

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UNITED STATES COURT OF APPEALS

For the Second Circuit

Docket No. 75-7008

STUART A. JACKSON,

Plaintiff-Appellant,

-against-

JACK OPPENHEIM,

Defendant-Appellee.

BRIEF OF DEFENDANT-APPELLEE

ISSUES PRESENTED

1. May a purchaser claim the right to recover from a seller under Section 12(2) of the Securities Act of 1933 where it is undisputed that the seller made no statements to the purchaser to effect the sale?

2. Where the purchaser has contracted to pay all counsel fees which might be incurred by the seller in enforcing

purchaser's promissory notes, was the trial court's award of attorney's fees to the seller proper in this case?

PRELIMINARY STATEMENT

Appellant Stuart A. Jackson, a lawyer, appeals from an adverse judgment entered by Honorable Charles H. Tenney, United States District Judge, after a three day trial before Judge Tenney, sitting without a jury.

The case before Judge Tenney, which alleged various violations of the federal securities laws, was unusual in two respects. First, the purchase and sale in question was between insiders of a private corporation. The seller, Jack Oppenheim, was an officer and director of that corporation. The purchaser, Jackson, also was an officer and director and, in addition, had acted as the corporation's outside counsel in various attempts to market the corporation's stock both before and after his purchase of a portion of Oppenheim's shares. Second, Oppenheim in essence did not "sell" his shares to Jackson. A dissident shareholder in a closely-held private corporation, Oppenheim agreed to sell all of his stock interest (146,183 shares) to and at the request of the controlling shareholders, Harold Steinberg and Andrew Norman. It was Steinberg, and not Oppenheim, who thereafter solicited Jackson's participation in what ultimately became a group of ten purchasers.

Jackson purchased 14,618 shares of the 146,183 share

block. He never spoke to Oppenheim about the purchase and Oppenheim never spoke to him. The sale of the entire 146,183 shares was closed on April 10, 1970. Payment was in cash and notes.

Thereafter, in March 1971, Jackson sued to rescind his part of the transaction, alleging violation of both Rule 10b-5 and Section 12(2) of the Securities Act of 1933. Jackson also brought action as counsel on behalf of one other of the ten purchasers. Oppenheim counterclaimed to collect on the promissory notes which included a provision for counsel fees. The case was tried on September 10-12, 1974. After hearing the evidence, including the testimony of both Oppenheim and Jackson, Judge Tenney dismissed Jackson's claim for rescission and ordered that judgment be entered in Oppenheim's favor on his counterclaim. This appeal follows.

STATEMENT OF FACTS

The securities in question were common stock of Chelsea House Educational Communications, Inc., a private corporation organized in 1966 to engage in publishing and in the production of educational films. The group was founded by Oppenheim together with Harold Steinberg, its President, and Robert Hector. Shortly after its formation, Andrew Norman became a major shareholder who, with Steinberg, owned a controlling interest in the corporation.

In early 1969 Steinberg approached the appellant Jackson with a view to retaining Royall, Koegel & Wells, the law firm of which Jackson was a partner. Royall, Koegel & Wells was retained as counsel by Chelsea House principally for the purpose of Jackson assisting in the preparation of material for a public offering of Chelsea House stock, and also for the purpose of Jackson helping Chelsea find an underwriter (A. 269-70, 491-94).

Indeed, in June 1969, when Jackson was elected Secretary and a Director of Chelsea House (Ex. 6, 7), Jackson was issued 12,500 shares of its common stock contingent upon success in obtaining an underwriter and effectuating a successful public offering (Ex. 2, p. 41).

Shortly after he had been retained, Jackson persuaded Price Waterhouse & Co. to become Chelsea House's independent auditors (A. 176) and introduced Chelsea House to the investment banking firm of Herzfeld & Stern (A. 168). Following a preliminary agreement by Herzfeld & Stern to underwrite a public offering of Chelsea House shares at $10 per share (A. 488), Royall, Koegel & Wells began work on a registration statement to be filed with the SEC (A. 132).

Under Jackson's supervision a registration statement and prospectus were prepared. Both as partner in charge

of the preparation of the registration statement and as a director of Chelsea House, Jackson conducted a line-by-line review of the statement, including the financials, and signed the final registration statement (A. 174, Ex. 2). Jackson also attended one or more meetings between representatives of Chelsea House and Herzfeld & Stern, the initial prospective underwriter, in connection with the proposed registration (A. 274).

The Chelsea House prospectus, as printed for filing, and which Jackson read and signed as partner in charge and as a Director, contained a lengthy statement of the nature of Chelsea House's business and the risks involved therein. The prospectus also included financial statements for Chelsea House's fiscal year ending October 31, 1968 (audited) and six months ended April 30, 1969 (unaudited). The prospectus explicitly disclosed that Chelsea House's sales and earnings to date were largely attributable to a single book, The 1897 Sears Roebuck Catalogue, that a substantial portion of Chelsea House's assets represented the capitalization of the costs of producing educational films for which no significant future sales could be assured, and that Chelsea House's future success was largely dependent on its ability to continue its financing and distribution arrangements with major book publishing and film organizations (Ex. C).

Herzfeld & Stern eventually took the position that it would go forward as underwriter <u>only</u> if the offering price to the public were reduced from the contemplated $10 per share to $7 per share. Chelsea House refused this reduction on the ground that the stock was worth $10 per share. Jackson knew of this refusal and of its reason (A. 274).

In late 1969 and early 1970 Jackson was aware of three further attempts to market Chelsea stock. In the fall of 1969 Jackson attended discussions between Chelsea House and Herbert Young & Co., a second underwriter whom Jackson himself helped introduce to Chelsea House (A. 178, 274, 471). Herbert Young & Co. proposed a public offering at $7 per share. Once again, Chelsea House refused this offer on the ground that the stock was worth at least $10 per share. Jackson was aware of this refusal and its reason (A. 274).

Soon after the failure of the Herbert Young & Co. negotiations, discussions commenced between Chelsea House and Bache & Co. with regard to Bache's assistance in connection with a private placement of the company's stock. At a meeting early January 1970, which Jackson's associate, Grant Anderson, attended at Jackson's direction, Bache withdrew its interest when it learned that Price Waterhouse's audit of Chelsea House's operations for its full fiscal year ended October 31, 1969 disclosed a net loss of $30,318. Anderson

reported Bache's withdrawal to Jackson and the reason therefor (A. 159-162).

In January 1970 Jackson, as a Director of Chelsea, received the final Price Waterhouse audited financial statement for the year ended October 31, 1969 (A. 183). Price Waterhouse's opinion in fact was qualified and was given only subject to the resolution of a $153,000 contingent liability and to the realization of $400,828 of film cost inventory, a significant portion of which pertained to uncompleted films and films for which there had been no material sales (Ex. B). Jackson read the statement including its footnotes (A. 182, 227).

In addition to revealing a highly precarious financial condition as of October 31, 1969, the audited statement, when compared with the unaudited six month figures contained in the earlier prospectus, demonstrated a clear and substantial negative turn-around in Chelsea's operations. It disclosed a net loss of $30,318 for the full year as compared with a net income of $127,724 for the first six months of that year. On a gross pre-tax basis, this reflected a loss from operations over the last six months of fiscal 1969 of an amount in excess of $284,000 as compared with a gross pre-tax profit for the first six months of that same year of approximately $254,000. It further revealed a decrease in net worth from $218,743 as of April 30, 1969 to

$85,097 as of fiscal year's end. It further showed a decrease in liquid assets (cash and current accounts receivable) from $234,976 to $139,513, and an increase in total "liquid" liabilities (current notes and accounts payable) from $271,557 as of April 30, 1969 to $667,192. Finally, it disclosed that Chelsea's gross sales, which had totalled $1,005,373 as of April 30, 1969, had increased only an additional $192,128, or, in effect, that Chelsea's gross sales for the last six months of fiscal 1969 had approximated only 20% or 1/5 of its gross sales for the first six months of that fiscal year (Ex. B).

The footnotes to the financial statements disclosed further significant facts bearing on Chelsea's liquidity. A majority of Chelsea's sales for the year were derived from a single book, The 1897 Sears Roebuck Catalogue. Receivables from the sale of two films had been assigned as security for a bank loan. Bank loans totalling $330,733 would come due by January 27, 1970. Chelsea had missed deadlines for the delivery of three manuscripts, and a failure to meet newly established deadlines would result in a cancellation of those contracts and a liability of $153,000. Finally, the books and films listed in inventory were largely unfinished and therefore did not represent potential revenue for payment of current debts (Ex. B).

In the months of January, February and March of 1970, Jackson had occasional conversations with members of Chelsea's day-to-day management, particularly Harold Steinberg. On these occasions Jackson asked no questions concerning the financial difficulties disclosed by Chelsea's year-end financial statement (A. 180, 513).

Before his purchase of Oppenheim's stock, Jackson also read an article in the March 2, 1970 edition of New York Magazine entitled "The Chelsea Boys and How They Grew" (A. 207, 416). The article, subtitled "The Zaniest Publishers in Town," portrayed the management of Chelsea House as irresponsible amateurs playing at publishing. A full-page picture accompanying the article shows Steinberg and Hector, then Chelsea House's President and Chairman, joking in Chelsea's offices with a topless secretary. In addition, the article noted Steinberg's proclivity for making the truth "elusive" and contained the following quotation from Steinberg concerning his methods of financing: "When you've set up the distributor and printer you get a royalty advance from the distributor and you pay the printer if you feel like it" (Ex. A).

Throughout the period from January of 1970 on, Oppenheim was openly critical of the performance of Chelsea House's management. On numerous occasions and to many officers and employees in Chelsea's offices--all or most of

whom were known personally by Jackson and to whom Jackson had access--Oppenheim voiced concern over the company's unstructured decision-making process, its fiscal irresponsibility, and the inability of its president, Steinberg, to inspire any confidence within the financial community. In his findings of fact Judge Tenney stated:

> "[T]he Court is inclined towards the view that defendant made a good faith effort to convince anyone who would listen, that Chelsea House was in a state of crisis. The problem, precisely, was that no one would listen--they generally considered defendant to be a gad fly, a complainer, and something of a nuisance." (A. 40).

Judge Tenney also found that "defendant was considered objectionable by those around him for his constant badgering about problems he perceived at Chelsea" (A. 48).

On March 13, 1970 Oppenheim met with Jackson in Jackson's office. Jackson and Oppenheim testified to sharply different recollections of this meeting. Judge Tenney resolved the issue <u>against</u> Jackson and found that Oppenheim went to Jackson's office "to complain about the management of Chelsea House and the inability of Chelsea House to acquire financing as a result of the alleged mismanagement" (A. 40). In that conversation, which lasted from fifteen minutes to half-an-hour, Oppenheim solicited Jackson's assistance in replacing Steinberg with someone who would inspire confidence within the financial community (A. 414-18).

Oppenheim also told Jackson that underwriters would not deal with Chelsea House so long as Steinberg was president, that the New York Magazine article had damaged Chelsea House's image in the financial community, that Chelsea House's financial problems were becoming increasingly severe, that the Christmas list of trade books had sold poorly, that Chelsea House's creditors were not getting paid, and that no definite sources of money were available to Chelsea House, either through its principal shareholder, Andrew Norman, or through a public offering (A. 414-18).

Within days after his conversation with Jackson, Oppenheim prepared a memorandum urging that Steinberg be replaced as president of Chelsea. Oppenheim gave copies of the memorandum to Robert Hector, chairman of Chelsea's board of directors, Leon Friedman, Chelsea's inside counsel, and Fred Israel, an editor and director of Chelsea House (A. 423-24). In addition, at least each of the following Chelsea employees read or were informed of the contents of the memo: Harold Steinberg, Andrew Norman, Harold Harris, and William Hansen (A. 69, 342). The memorandum itself requested the scheduling of a meeting of the board of directors to vote on Oppenheim's recommendation (Ex. 1).

As part of its advocacy of the replacement of Harold Steinberg, Oppenheim's memorandum argued that Chelsea

"is going through a period in which the question of its survival may be at stake." The memorandum stressed the company's difficulty in meeting its current debts, the irresponsibility of its management, and the company's need to enlist outside capital. In support of his points, Oppenheim gave specific examples. He mentioned the 1969 loss, the fact that Chelsea's net worth was under $100,000, the failure of Chelsea's Christmas list of trade books, and the avoidance of creditors (Ex. 1). The main points were criticisms which Oppenheim had voiced in the company's offices on prior occasions (A. 343). They were facts or incidents which were generally known among Chelsea's officers and principal employees (A. 405, 410, 419). For instance, Chelsea had always had difficulty paying its debts as they came due (A. 90). The memorandum set forth essentially the same argument in favor of Steinberg's replacement that Oppenheim had made to Jackson, except that the memorandum provided greater detail by way of examples (A. 422).

Some time at the end of March 1970, Oppenheim was approached by a Chelsea House employee named William Poten, who asked if Oppenheim would be willing to sell out his shares in Chelsea House. When Oppenheim said that he would, negotiations began (A. 443, 445). Poten acted as an intermediary between Oppenheim as seller and Steinberg and Norman,

the controlling shareholders. The basic terms of the sale were set in this manner. Steinberg and Norman then assembled an initial group of purchasers with Norman to take the largest number of shares (A. 541). Oppenheim solicited none of these purchasers (A. 479, 483). He made absolutely no statements or representations in connection with the sale, misleading or otherwise (A. 479-485).

At some time later in March or early in April, 1970, Steinberg called Jackson and told him that certain members of Chelsea House's management were buying out Oppenheim's shares at a price of $3 per share. Jackson asked Steinberg how Chelsea House's business was doing. When Steinberg replied that "business was good," Jackson told Steinberg that he would take the same number of shares that Steinberg was taking. Jackson, who had read Price Waterhouse's audited statement for Chelsea's fiscal year ending October 31, 1969, asked no questions about it (A. 219). Indeed there was no other discussion between Jackson and Steinberg of Chelsea's business or financial condition or of the purchase of Oppenheim's shares (A. 83-86, 187, 510-512).

Jackson assigned Grant Anderson to go to Steinberg, to get from him the terms of the purchase which already had been negotiated, and to prepare the legal documents necessary to consummate the transaction. Anderson consulted with

Steinberg and the attorney representing Oppenheim and then prepared documents on behalf of all persons participating in the purchase of Oppenheim's stock. Anderson billed his time to Chelsea and not to Jackson (A. 136, 163).

From the time of Jackson's conversation with Steinberg to the date of the closing, Jackson made no inquiries either of Oppenheim, of the other purchasers, or of any Chelsea officer or employee as to Chelsea House's financial condition (A. 273, 282). He also made no inquiry of Price Waterhouse which, at Jackson's own request of Steinberg, were then in the process of preparing up-dated audited financials (A. 263). Oppenheim likewise made no statements to Jackson.

Significantly, Jackson did not tell Oppenheim that Jackson, in February 1970, had introduced Chelsea House to the investment banking firm of E.L. Aaron & Co. Jackson had been present at a meeting between Chelsea House and Aaron representatives at which a possible underwriting was discussed. Oppenheim had not there and did not know of the proposed underwriting. Although at the time of his purchase of Oppenheim's shares Jackson knew that underwriting negotiations were being carried on between Chelsea and E.L. Aaron & Co. (A. 277-8, 294), at no time during this period did Jackson or anyone else disclose to Oppenheim the existence

of such negotiations (A. 99, 129). Subsequent to the sale of Oppenheim's shares, Chelsea House and E.L. Aaron in fact signed a letter of intent for a "best efforts" underwriting of Chelsea House stock at $7.00 per share, $4.00 per share more than Oppenheim had received (Ex. E).

At all relevant times Jackson had access to the books, records, officers, and independent auditors of Chelsea House at least equal to Oppenheim's (A. 325).

On April 10, 1970 pursuant to an agreement involving 10 purchasers, Jackson purchased 14,618 shares of Oppenheim's Chelsea House stock (Ex. H). Jackson paid $10,000 down and delivered two promissory notes, each in the amount of $16,962 payable respectively in one and two years, with interest at 9 1/2% with provisions for payment by the maker of all costs of collection, including counsel fees (A. 31, Ex. I).

After the transaction Chelsea House continued to have difficulty in obtaining financing to pay its current debts, and on July 2, 1970 it filed a petition for reorganization pursuant to Chapter 11 of the Bankruptcy Law (A. 31). In a petition filed thereafter in support of his law firm's claim for legal fees, Jackson swore that as outside counsel he had been "well-acquainted" with Chelsea House's business and financial condition at all relevant times (A. 283-284; Exh. F).

POINT I

THE DISMISSAL OF JACKSON'S SECTION 12(2) CLAIM WAS PROPER

The entire thrust of Jackson's claim, as presented to Judge Tenney, was based upon Oppenheim's alleged violation of Rule 10b-5. In essence, Jackson urged that Oppenheim "willfully had failed to disclose the deteriorating financial condition of Chelsea House" to Jackson's detriment (A. 6). Jackson's concentration on Rule 10b-5 was so intense that his Section 12(2) claim, which forms the _only_ basis of his appeal to this Court, was not even briefed in his post-trial memorandum submitted to Judge Tenney.

Judge Tenney, who heard and observed all of the witnesses, including Jackson and Oppenheim, rejected Jackson's claim on several grounds. He found, _inter alia_, that Jackson had failed to establish that he would not have participated in the purchase had he read Oppenheim's memorandum and, moreover, that Jackson in any event either knew or had equal and easy access to everything Oppenheim knew, had more than sufficient notice of Chelsea's condition, and failed to exercise even a semblance of that due care required of an investor in the circumstances.

In support of this last determination, Judge Tenney quite logically pointed to Jackson's position as an officer, director, and outside counsel to Chelsea, his responsibility for and review of its registration statement, his instrumental assistance and participation in the various abortive underwritings, his relationship to Price Waterhouse and knowledge of PW's audited year-end financials, his admitted high degree of sophistication, his reading of the clearly uncomplimentary New York Magazine article about Chelsea shortly before his participation in the block purchase, and his sworn statement, filed in support of his law firm's petition for legal fees, that at all relevant times Jackson was "fully familiar" with the business of Chelsea House and its financial condition.

Moreover, contrary to Jackson's testimony, Judge Tenney found that on March 13, 1970 Oppenheim told Jackson of his complaints with Chelsea's management and of Chelsea's inability to obtain financing as a result of this mismanagement (A. 40). Finally, as to Oppenheim, Judge Tenney found that he had made his views known time and again, and that there was "simply no evidence of his bad faith" (A. 40). The short of the matter is that Judge Tenney, who heard Jackson and Oppenheim testify, flatly rejected Jackson's claim that Oppenheim had committed fraud.

It seems significant that Jackson, who relied exclusively upon Rule 10b-5 below, no longer contests Judge Tenney in this respect. Rather, in a somewhat abrupt change of direction, Jackson in this Court has abandoned his 10b-5 claim and argues only that he should have recovered under Section 12(2) of the Securities Act of 1933.

Jackson's claim is that Section 12(2) -- like Rule 10b-5 -- creates a right of action based on silence, but -- unlike Rule 10b-5 -- allows for none of the defenses successfully interposed by Oppenheim. In essence, Jackson urges that Section 12(2) sanctions recovery in circumstances where Rule 10b-5 does not and, in effect, is broader in scope and more punishing in impact. His argument is quite misleading, ignores the clear language of Section 12(2), and grievously distorts the meaning and purpose of that statute.

What Jackson conveniently ignores is that Section 12(2) reaches statements only. It creates no cause of action based upon silence. Unlike certain provisions of Rule 10b-5, namely, subdivisions (1) and (3), which impose an affirmative obligation of disclosure in certain circumstances, Section 12(2) gives rise to liability <u>only</u> where an offer or sale of securities is effected by means of a statement which is either false or is misleading because it is only half true.

The language of Section 12(2) could not be clearer in this regard. It prohibits the offer or sale of a security:

> ". . . by means of a prospectus or oral communication which includes an untrue statement of a material fact or omits to state a material fact necessary in order to make the statements, in the light of the circumstances, under which they were made, not misleading . . ."

Quite simply, Section 12(2) applies only to <u>actual statements</u> which either are "untrue" or half-true. Silence, i.e., an omission to state, is actionable only where there has been an actual statement which is misleading because of the omission. But there must first be a statement.

The undisputed evidence is that Oppenheim made no statement whatsoever to Jackson in connection with the offer or sale of his stock. Jackson entered the purchasing group at the invitation of others. He never spoke to Oppenheim about the sale and Oppenheim never spoke to him. Indeed Jackson fails even to allege a statement by Oppenheim to him in this connection, and certainly no evidence of any such statement was offered. And Judge Tenney, on all the evidence, found that Oppenheim at all times acted in complete good faith.

Courts and commentators have recognized that § 12(2) applies only to actual statements. The discussions

have arisen principally in the context of an analysis of the identical statutory language which appears in subparagraph (2) of Rule 10b-5 and in § 17(a)(2) of the Securities Act. For example, in Trussell v. United Underwriters, Ltd., 228 F. Supp. 757, 767 (D. Colo. 1954), the court held:

> "Section 17(a)(2), as well as Rule 10b-5(2) is specifically aimed at half-truths. Both of these provisions are limited to half-truths, as distinct from complete omissions to disclose anything. They do not require the seller 'to state every fact about stock offered that a prospective purchaser might like to know or that might, if known, tend to influence its decision.' Otis & Co. v. S.E.C., 106 F.2d 579, 582 (6th Cir. 1939). Section 17(a)(2) and Rule 10b-5(2) both contain a requirement that some statement be made. Although a course of action violative of §§ 17(a)(1) or 17(a)(3) will usually be violative of § 17(a)(2)--and necessarily contain the element of scienter on the part of the defendant seller as well--it is possible that §§ 17(a)(1) or 17(a)(3) will encompass a scheme to defraud based upon silence, which would not always be cognizable as common-law deceit, giving effect to the principles outlined in §§ 550 and 551 of the Restatement of Torts (1938). Although § 12(2) appears to create no express civil remedy available to a purchaser who has been injured by such a scheme, the purchaser does have available an implied remedy under Rule 10b-5(1) and Rule 10b-5(3)."

The same reading of this language has been made in this Circuit. In List v. Fashion Park, Inc., 340 F.2d 457, 462 (2d Cir.), cert. denied, 382 U.S. 811 (1965), this Court said,

> "It may well be that suits under Rule 10b-5 involving total non-disclosure cannot be brought pursuant to clause (2) of the rule."

Similarly, in Cochran v. Channing Corp., 211 F. Supp. 239, 243 (S.D.N.Y. 1962), the court held:

> "The fact that the defendants did not make any statements at all does not, in and of itself, deprive plaintiff of relief. The three subsections of Rule 10b-5 are in the disjunctive, and while subsection (2) seems to require a statement of some sort, subsections (1) and (3) do not."

See also, L. Loss, 3 Securities Regulation 1439, 1702 (1961).

Strangely, in his own brief on this appeal, Jackson at first properly states that liability under Section 12(2) arises only upon evidence which establishes that "the defendant made an untrue statement of a material fact or omitted to state a material fact necessary in order to make the statements, in light of the circumstances under which they were made, not misleading" (Jackson Br. p. 17). The short of it is that Jackson concedes in his own brief

that a Section 12(2) violation cannot exist in the absence of a statement, as we submit. Indeed every case cited by Jackson involved a false statement or half-truth. Yet, as is clear from all the evidence, Jackson failed entirely to establish any statement by Oppenheim "by means of" which the stock was sold, and indeed concedes the absence of any such statement.

Jackson nonetheless does attack Judge Tenney's determination of his Section 12(2) claim by taking issue with Judge Tenney's finding that Oppenheim had "exercised reasonable care" to avoid any omission of any material fact which might have misled Jackson. But, since the evidence established without dispute that Oppenheim did not offer or sell stock to Jackson "by means of" a false statement or half-truth, Judge Tenney clearly was correct in his determination that Oppenheim had exercised all reasonable care not to mislead Jackson. Oppenheim obviously could not have omitted any material facts to Jackson's detriment under Section 12(2), since Oppenheim made no statements to Jackson either to solicit Jackson's participation in the block purchase, or to promote the block purchase itself. Indeed, the evidence is clear that it was other insiders, namely, Steinberg and Norman, who suggested that Oppenheim sell out his stock, who

negotiated that sale with Oppenheim, and who thereafter solicited Jackson's participation in the purchasing group. There simply was no evidence in this case of bad faith on Oppenheim's part in connection with the sale.

Finally, even if this Court were to find for the first time that some sort of affirmative disclosure requirement exists under Section 12(2) in the absence of a statement, Judge Tenney's dismissal of Jackson's claim in this regard was equally correct. As this Court held in another context in Frigitemp Corp. v. Financial Dynamics Fund Inc., CCH Fed. Sec. L. Rep. ¶ 95,323 (2d Cir. 1975) at 98,636:

> "Whether 'constructive knowledge,' or 'ready access to the information involved,' City National Bank v. Vanderboom, 422 F.2d 221, 231 (8th Cir. 1970), is always a bar to the plaintiff we need not decide. Suffice it to say that even if we lower the requirement of scienter on the part of the defendant, see discussion in Lanza v. Drexel & Co. 479 F.2d 1277 (2d Cir. 1973) (en banc), his reasonable belief that the other party already has access to the facts should excuse him from new disclosures which reasonably appear to be repetitive."

Applying this standard to the evidence in this case, Oppenheim is without fault even if a requirement of affirmative disclosure is read into Section 12(2) for the

first time. Oppenheim's views with regard to the situation at Chelsea were all but broadcast to the world, and the substance and much of the detail of his memorandum had in fact been disclosed to Jackson during their meeting on March 13, 1970. It is hard to conceive of a record which more clearly establishes the good faith and reasonable care of a seller such as Oppenheim. Judge Tenney's findings suffice (A. 39, 40):

> "Plaintiff makes no allegation that defendant made untrue statements. Rather, plaintiff alleges an omission to state material facts, namely that defendant failed to provide him with a copy of the March 1970 memorandum, and further, that defendant did not know whether plaintiff had received a copy from another source."
>
> * * *
>
> "This Court is not convinced, based on the evidence presented, that defendant acted in a manner which exhibited a willful or reckless disregard for the truth. Rather, the Court is inclined toward a view the defendant made a good faith effort to convince anyone who would listen, that Chelsea House was in a state of crisis. The problem, precisely, was that no one would listen--they generally considered defendant to be a gadfly, a complainer, and something of a nuisance."
>
> * * *

"[Defendant] made a reasonable attempt to distribute the memorandum. More importantly, perhaps, there is no evidence that he made any attempt to limit distribution of the memorandum or to limit access to any part of it. Defendant had made his views known time and again. There is simply no evidence of his bad faith."

POINT II

THE AWARD OF COUNSEL FEES TO OPPENHEIM WAS PROPER

Having dismissed Jackson's claims, Judge Tenney enforced the notes given to Oppenheim in partial payment for the Chelsea House stock at issue. These notes, sued upon by Oppenheim in his counterclaim, provide for payment not only of the principal amount but also of costs of collection. Such costs expressly include attorneys' fees:

> "If this note is placed with an attorney for collection the maker shall pay all costs of collection, including, but not limited to, counsel fees, which fees shall be added to the unpaid balance of this note and be recoverable with and as part thereof" (Ex. I).

Although collection costs provisions are common and routinely enforceable, cf. Uniform Commercial Code § 3-106(e), Jackson argues that they should not be enforced here. He maintains first that attorneys' fees may not be awarded in a securities case in the absence of an explicit finding that the securities claim borders on frivolity or is brought in bad faith. Second, he claims that a contractual term such as this should not be enforced where a securities law defense, albeit without merit, is raised. Neither argument has substance.

Judge Tenney's award of attorneys' fees here was not pursuant to his discretionary power to award such fees as _costs_ where a securities claim borders on frivolity or is brought in bad faith, although we believe the facts here would support such an award. Counsel fees here were awarded as an element of _damages_ pursuant to a contractual provision which specified the damages Oppenheim would be entitled to in the event that Jackson defaulted on his notes. The cases cited by Jackson in support of the "frivolity" standard are therefore wholly off point; none of them purport to limit a noteholder's right to attorneys' fees as damages. They merely state the standard for the Court's discretionary award of counsel fees as costs.

The mere fact that Oppenheim was forced to defend against a securities claim in order to collect on his notes does not vitiate the collection costs provision. Such a provision is enforceable whether or not the holder is compelled to seek collection by counterclaim to an action for rescission under the securities laws. _Tartell_ v. _Chelsea National Bank_, 351 F. Supp. 1071 (S.D.N.Y.), _aff'd_, 470 F.2d 994 (2d Cir. 1972); _Jaeger_ v. _Canadian Bank of Commerce (California)_, 327 F.2d 743 (9th Cir. 1964); _Taylor_ v. _Continental Supply Co._, 16 F.2d 578 (8th Cir. 1926).

In _Tartell_ Judge Tyler enforced a collection costs provision despite "the facts that (1) plaintiff won the race to the Federal courthouse door and (2) plaintiff's suit was predicated on Federal statutory law." 351 F. Supp. at 1079. That holding is controlling on the issue raised here.

The _Tartell_ holding is also supported by decisions in other circuits. In _Jaeger_, _supra_, the Ninth Circuit held that the holder of a note could recover the costs not only of its suit for collection but also of its defense against a counterclaim which was not related to the maker's indebtedness. The Court relied on _Taylor_ v. _Continental Supply Co._, _supra_, a case in which the counterclaim was related to the note. It said:

> "[T]here is a fundamental similarity between the two cases because unless plaintiff was willing to yield to the defendant on the issue of attorneys' fees, it was obliged to dispose of the counterclaim in order to secure judgment on its note." 327 F.2d at 746.

In _Taylor_ the Eighth Circuit said:

> "To collect the notes it was necessary to bring suit and to defend against the counterclaim . . . if it is not true that attorneys' fees can be collected in defense of a counterclaim where it is sought to offset the amount due on a note when suit is brought thereon, then the provision for attorneys' fees would be of little force or affect, and easily circumvented." 16 F.2d at 580-81.

See also, Corpus Juris Secundum Bills and Notes § 726(6):

> "Under a stipulation in a note or in an agreement with reference thereto to the effect that attorneys' fees will be allowed if suit is brought, such fees may be recovered for the defense of a counterclaim and negotiating a settlement after suit has been filed on the note, or for the filing of a claim against the estate of the maker, where the claim is resisted, or for the prosecution of a cross bill."

Jackson has cited only a single case to support his argument that a securities claim, even unfounded, should nullify a collection costs provision. That case, Sackett v. Beaman, 399 F.2d [illegible]84, (9th Cir. 1968), is not in derogation of the rule stated in the cases cited above, for in Sackett the defendant in the securities action did not counterclaim to enforce his note as Oppenheim did here. In fact, Oppenheim had no other choice for Rule 13(a) Fed. R. Civ. P. requires that a defendant raise any claim he might have against an opposing party that arises out of the transaction or occurrence that is the subject matter of the opposing party's claim.

Enforcement of the collection costs provision here is not only required by the cases but it is also fair and appropriate. Such provisions are intended to indemnify the creditor against the cost of enforcing his rights, and

to avoid the possibility that economic pressures may force a waiver and loss thereof. Collection costs provisions are commercially useful in debt transactions so as to reduce the risk involved in taking payment in a form other than cash. Given the purpose of the collection costs provision, it is clear that the parties' intent was to indemnify Oppenheim whether or not collection was opposed and whether or not the maker of the note initiated suit first.

For all of the above reasons, Judge Tenney's award should be upheld.

CONCLUSION

The judgment below should be affirmed.

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Respectfully submitted,

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